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TREASURY, DEPARTMENT OF

A delay in the implementation date for testing plans for compliance with section 89 regulations was announced 5/1/89 by Secretary of the Treasury Nicholas F. Brady. He said the section 89 regulations would not be implemented until 10/1/89. The Secretary made the announcement in an address to the U.S. Chamber of Commerce in Washington, D.C. Secretary Brady said he has also asked Congress to work with the Administration "to find ways to revise section 89 to make its requirements less burdensome to businesses." He said, "The authors of this law intended that it assure an equitable system of health benefits for all workers. But in attempting to issue the section 89 regulations, the Treasury Department has found it imposes unreasonable compliance burdens on business. The cost of compliance with section 89, as it presently stands, is excessive. The law needs to be changed and we stand ready to encourage, support and work with Congress to revise and improve it."

In a related action, in 5/2/89 testimony before the House Ways and Means Committee, Dana L. Trier, tax legislative counsel for the Department of Treasury, said, "The special circumstances faced by small businesses should be addressed in any legislation enacted to modify section 89...Congress should consider alternative ways in which small businesses that cannot purchase health insurance at favorable group rates may comply with the nondiscrimination rules...The Administration suggests...that Congress consider permitting small businesses to satisfy the nondiscrimination rules under alternative tests. A small business for this purpose would generally be defined as a business with ten or fewer employees. However, an employer with a larger number of employees could, under rules developed by the Secretary of the Treasury, be granted similar relief to the extent it was found that the employer faced similar circumstances in purchasing insurance." (See related story in this issue of the Wash. Rpt. about the AICPA's testimony at this hearing.)

The application of the tax benefit rule to the minimum tax is the subject of temporary and proposed rules issued by the IRS (see the 5/5/89 Fed. Reg., pp. 19363-72 and pp. 19409-10). The IRS said the regulations provide taxpayers with guidance necessary to determine the amount of tax preference items that do not provide a current tax benefit because of available credits, and therefore, are not subject to minimum tax. The temporary and proposed regulations generally are effective for items of tax preference that are subject to the minimum tax imposed by section 56 of the Internal Revenue Code and arise in taxable years beginning after 12/31/75 and before 1/1/87. Except as otherwise provided, the regulations do not apply for purposes of determining alternative minimum tax liability imposed by section 55 of the Code. Section 1.58-9T(a) of the regulations provides that under section 58(h) of the Code taxpayers are not liable for the minimum tax imposed by section 56 on tax preference items from which no current tax benefit is derived because available credits would have reduced or eliminated the taxpayer's regular tax liability if preference items had not been allowed in computing taxable income. Section 1.58-9T(a) of the temporary regulations further provides that any credits that, because of such preference items, are not needed for use against regular tax ("freed-up credits"), are required to be reduced under the rules of section 1.58-9T(c) of the regulations. Section 1.58-9T(c) of the regulations provides that a taxpayer's freed-up credits must be reduced by the additional minimum tax that would have been imposed if a current tax benefit had been derived from preference items that did not actually produce a current tax benefit. The regulations also provide the method for calculating the reduction. In addition, the regulations include rules necessary to allocate properly the required credit reduction among credits that are of more than one type or that were earned in more than one taxable year. The IRS said these rules take into account the order in which such credits would have been applied to

offset the additional tax that would have been imposed if preferences had not been allowed, percentage limitations that would have affected the use of such credits against this additional tax, and the marginal rates at which this additional tax would have been imposed. Written comments and requests for a public hearing must be delivered or mailed by 7/5/89. For further information after reading the temporary and proposed regulations, contact William A. Jackson at the IRS at 202/566-4196.

The allocation and apportionment of losses incurred by banks with respect to certain loans made in the ordinary course of the bank's trade or business is the subject of guidance under section 865 of the Internal Revenue Code issued by the IRS in Notice 89-58. The IRS said that generally the notice provides that losses recognized with respect to such loans shall be allocated to the class of interest income generated by such instruments, and shall be apportioned between US source interest income and one or more separate limitation categories of foreign source interest income included within the class of interest income. The losses must be apportioned according to an asset method of apportionment that is based on the outstanding amount of loans generating interest income in such groupings. Definitions of banks, affiliated corporations, and eligible loans are included in the notice. The IRS also said that the rules included in Notice 89-58 will be incorporated in regulations to be promulgated under section 865 of the Code. Notice 89-58 is effective for taxable years beginning after 12/31/86. Notice 89-58 is scheduled to be published in Internal Revenue Bulletin 1989-20, dated 5/22/89. For further information after reading the notice, contact Carol P. Tello at the IRS at 202/377-9433.

Revised valuation tables for valuing transfers of interests in property made after 4/30/89 were released recently by the IRS in Notice 89-60. The tables contain actuarial factors to be used in determining the present value of an annuity, an interest for life or for a term of years, or a remainder or reversionary interest. The issuance of the new tables was mandated by the Technical and Miscellaneous Revenue Act of 1988. The law also required that the new tables be based on an interest rate that is 120 percent of the applicable Federal midterm rate for the month in which the valuation date falls and the most recent mortality experience available. In Notice 89-24, which was published in Internal Revenue Bulletin 1989-10, dated 3/6/89, temporary guidance was provided in planning transfers that would take place after 4/30/89 (see the 2/27/89 Wash. Rpt.). Notice 89-24 provides formulas for computing the value of transferred interests based on the appropriate applicable Federal midterm interest rate and the prior mortality experience. The IRS said the tables and formulas contained in Notice 89-60 apply to the valuation of interests in property for income, estate, gift, and generation-skipping transfer tax purposes in the cases of decedents dying after 4/30/89, and gifts and certain other transfers made after that date. The IRS said a complete set of tables, including two life and additional single life factors, will be published soon. Notice 89-60 is scheduled to be published in Internal Revenue Bulletin 1989-22, dated 5/30/89. For further information after reading the notice, contact William L. Blodgett at the IRS at 202/377-9661.

Walter D. Duvall, CPA, has been appointed regional inspector for the IRS Mid-Atlantic Region headquartered in Philadelphia, the IRS announced. As regional inspector, Mr. Duvall is responsible for all IRS inspection activities conducted by the internal audit and internal security divisions in PA, NJ, DE, MD, DC, VA, and all IRS foreign posts of duty. The IRS said the internal audit division

independently reviews operations to insure that the duties of the IRS are carried out properly. The internal security division investigates allegations of bribery, impersonations of IRS personnel, assaults and threats against IRS employees, embezzlement, and employee misconduct. Mr. Duvall began his IRS career in 1970 as an internal auditor in Austin, TX. In 1971, he joined the internal audit staff in Washington. In 1976, Mr. Duvall became program manager at the office of the regional inspector in the IRS Central Region, headquartered in Cincinnati. He was named assistant regional inspector for the Mid-Atlantic Region in 1984, the position he held until his present appointment.

A magnetic tape filing program for certain employee pension plan returns and related schedules will be conducted during the 1989 filing period, the IRS announced (see the 5/1/89 Fed. Reg., p. 18625). Filing returns on magnetic tape will eliminate most manual processes required by IRS to handle paper documents and will help "improve the accuracy of returns, speed up processing, and minimize the need for correspondence," the IRS said. Forms 5500-C, 5500-R and related Schedules A, B, P, and SSA are included in the program. The IRS said the program will be available nationwide and will be processed at the IRS Center in Andover, MA. Tax practitioners and other interested parties can obtain copies of the draft revenue procedure for the program by writing or calling: Internal Revenue Service Center, 310, Lowell Street, Andover, MA 01812, Attn: Electronic Filing Unit, Stop 981, 508/474-9441. Applicants wishing to participate must send a letter by 6/15/89 requesting acceptance into the program to the above address. The letter must include the name of the plan sponsor and employer, if for a single employer plan; address; contact person's name; daytime telephone number; and the types of forms and schedules that will be filed.

SPECIAL: HOUSE BANKING COMMITTEE APPROVES SAVINGS AND LOAN RESCUE LEGISLATION

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989, which was approved by the House Banking, Finance, and Urban Affairs Committee on 5/2/89, includes language requiring independent annual audits for all federally insured institutions and management reports to Federal regulators on its internal controls and on compliance with laws and regulations relating to safety and soundness. The independent auditor would be required to report on management's assertions regarding its internal controls and its compliance with certain specific laws and regulations related to safety and soundness. The language was added during full committee markup of the measure, H.R. 1278, after a different version of the provision was defeated by the subcommittee. The amendment, which originated from a General Accounting Office proposal, was offered by Rep. Toby Roth (R-WI). The provision would require federally insured institutions with assets of more than \$150 million to obtain independent audits of their financial statements each year. H.R. 1278 will next be referred to the House Ways and Means and Judiciary Committees for consideration of the bill's provisions over which the committees have jurisdiction. H.R. 1278 must also be approved by the full House. Following House approval, a House and Senate conference committee will meet to resolve differences between the House and Senate versions of the legislation.

SPECIAL: HOUSE SUBCOMMITTEE HOLDS RICO HEARING

The first in a series of hearings on legislation to revise the Racketeer Influenced and Corrupt Organizations Act (RICO) was held 5/4/89 by the House Judiciary Subcommittee on Crime. The specific focus of the hearing was H.R. 1046, which

was introduced 2/22/89 by Rep. Rick Boucher (D-VA) (see the 2/27/89 Wash. Rpt.). At the hearing, Subcommittee Chairman William J. Hughes (D-NJ) said that this was the first of several hearings that he would hold, but that he planned to move "expeditiously" on the issue. He said he does not want to see consideration of the legislation drag on until the final days of the 101st Congress and then be stalled because of lack of time to consider anything other than essential legislation, as has happened during the past two Congresses. Rep. Hughes also remarked that attendance by every member of the Subcommittee at the hearing indicated a high level of interest by the Subcommittee in amending RICO.

SPECIAL: AICPA SUPPORTS MODIFYING CHAIRMAN ROSTENKOWSKI'S SECTION 89 BILL

The Tax Division of the AICPA generally supported the approach to simplification of section 89 contained in H.R. 1864 in testimony presented to the House Ways and Means Committee at a 5/2/89 hearing on the measure, but also suggested modifications which would make the bill fairer to employers and employees. H.R. 1864 was introduced by Rep. Dan Rostenkowski (D-IL), chairman of the Ways and Means Committee (see the 4/17/89 Wash. Rpt.). The testimony was presented by Arthur S. Hoffman, chairman of the AICPA Federal Taxation Executive Committee. He said the Tax Division particularly supported the measure's focus on plan availability rather than plan coverage, but supported changes in the treatment of cafeteria plans and the appropriate indexing of employee contributions for a qualified core health plan. Mr. Hoffman cited "hundreds of calls" the AICPA has received from CPAs across the country which disclosed that "taxpayers are unable or unwilling to understand section 89's rules." He said, "Employers are seriously considering whether to eliminate some or all of the employee health coverage. Others plan to eliminate the tax deferred health coverage." Mr. Hoffman also pointed out to the Committee the increased cost of complying with section 89 for employers and he predicted a growing enforcement problem for the IRS in ensuring compliance.

Mr. Hoffman identified the following as three of the more significant recommendations being made by the AICPA: 1) Since it is generally thought that H.R. 1864, as presently drafted, would have a negative impact on cafeteria plans, health benefits provided under cafeteria plans should be excluded from discrimination tests, and discrimination should be determined by a benefits test; 2) H.R. 1864 provides that the \$10/\$25 limits of the affordability standard would be adjusted in the future as wages increase. The AICPA recommended using a percentage of an employee's wages as a means of adding flexibility to the affordable plan proposed in H.R. 1864. The Institute suggested that the maximum contribution for each employee should be 40 percent of the premium cost or 5 percent of that worker's wages. This would allow employees to share in the increased cost of health care while at the same time protecting the very low income worker; and 3) Four modifications were suggested by the AICPA as possible ways to correct the "inequities" for employers who are slightly below the cutoff for the 90 percent eligibility test: lower the percentage; include a graduated penalty schedule; eliminate leased employees from the calculation; or provide a grace period for employers who substantially meet the eligibility rules.

Mr. Hoffman concluded his testimony by stating, "The AICPA believes that modification of section 89 is absolutely necessary and applauds the Chairman's efforts towards this end as manifested in H.R. 1864. We think that the changes we have recommended...will result in a fairer, more workable and more enforceable law."

SPECIAL: JOINT TAX COMMITTEE RELEASES PAMPHLET ON BILLS AND ISSUES RELATING TO SECTION 89

"Description of Certain Bills and Discussion of Issues Relating to Section 89 Nondiscrimination Rules Applicable to Certain Employee Benefit Plans" is the title of a new pamphlet issued by the Joint Committee on Taxation. The pamphlet was prepared by the Committee staff in connection with the 5/9/89 hearing scheduled by the Senate Finance Committee on section 89 (see the 4/17/89 Wash. Rpt.). The pamphlet provides a description of present-law section 89 rules, a description of selected bills relating to section 89, and a discussion of issues related to nondiscrimination rules for employer-provided accident or health plans. The pamphlet (JCS-10-89) is available at a cost of \$1.00 from the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402-9325. The pamphlet is GPO Stock No. 052-070-065-72-9. Checks or money orders should be made payable to the Superintendent of Documents.

For further information contact Shirley Twillman at 202/737-6600.

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1455 Pennsylvania Ave., NW, Washington, D.C. 20004-1007

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